



Sonnenberg & Company, CPAs

A Professional Corporation

5190 Governor Drive, Suite 201, San Diego, California 92122

Phone: (858) 457-5252 • (800) 464-4HOA • Fax: (858) 457-2211 • (800) 303-4FAX



Leonard C. Sonnenberg, CPA

HOME START, INC.
Audited Financial Statements
Single Audit Reports
June 30, 2008

DATE RECEIVED:



AUDIT REVIEW #(s) 04555

Assigned To: Leahy

Date Reviewed: 4/2/09

Reviewer's Initials: SL

Date Review(s) Completed: 4/9/09

HOME START, INC.
TABLE OF CONTENTS
June 30, 2008

	<u>Pages</u>
INDEPENDENT AUDITOR'S REPORT ON THE FINANCIAL STATEMENTS	1
FINANCIAL STATEMENTS	
Statement of Financial Position	2
Statement of Activities	3
Statement of Functional Expenses	4
Statement of Cash Flows	5
Notes to Financial Statements	6-10
ADDITIONAL INFORMATION	
Schedule of Expenditures of Federal Awards	11
Auditor's Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with <i>Government Auditing</i> <i>Standards</i>	12-13
Auditor's Report on Compliance with Requirements Applicable to Each Major Program and on Internal Control Over Compliance in Accordance with OMB Circular A-133	14-15
Schedule of Findings and Questioned Costs	16-18



Sonnenberg & Company, CPAs

A Professional Corporation

5190 Governor Drive, Suite 201, San Diego, California 92122

Phone: (858) 457-5252 • (800) 464-4HOA • Fax: (858) 457-2211 • (800) 303-4FAX



Leonard C. Sonnenberg, CPA

INDEPENDENT AUDITOR'S REPORT ON THE FINANCIAL STATEMENTS

To the Board of Directors of
Home Start, Inc.

We have audited the accompanying statement of financial position of Home Start, Inc. (a Nonprofit Organization) as of June 30, 2008, and the related statements of activities, functional expenses, and cash flows for the year then ended. These financial statements are the responsibility of Home Start, Inc.'s management. Our responsibility is to express an opinion on these financial statements based on our audit. The prior-year summarized comparative information has been derived from Home Start, Inc.'s June 30, 2007 financial statements which were audited by us, and, in our report dated November 21, 2007, we expressed an unqualified opinion on those financial statements.

We conducted our audit in accordance with U.S. generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Home Start, Inc. as of June 30, 2008, and the changes in its net assets and its cash flows for the year then ended in conformity with U.S. generally accepted accounting principles.

In accordance with *Government Auditing Standards*, we have also issued our report dated October 30, 2008 on our consideration of Home Start, Inc.'s internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, grants, agreements, and other matters. The purpose of that report is to describe the scope of our testing of internal controls over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in assessing the results of our audit.

Sonnenberg & Company, CPAs

October 30, 2008

HOME START, INC.
Statement of Financial Position
June 30, 2008
(With Summary Totals for June 30, 2007)

	<u>2008</u>	<u>2007</u>
OPERATING ASSETS:		
Cash	\$ 66,670	\$ 10,519
Accounts Receivable	1,452,441	1,494,668
Prepaid Expenses	235	27,402
Deposits	<u>14,415</u>	<u>15,112</u>
Total Operating Assets	1,533,761	1,547,701
FIXED ASSETS:		
Computer Equipment	88,406	88,406
Furniture & Fixtures	70,970	70,970
Leasehold Improvements	14,942	14,942
Vehicles	13,841	13,841
Accumulated Depreciation	<u>(143,260)</u>	<u>(123,911)</u>
Total Fixed Assets	<u>44,899</u>	<u>64,248</u>
TOTAL ASSETS	<u><u>\$ 1,578,661</u></u>	<u><u>\$ 1,611,949</u></u>
LIABILITIES:		
Accounts Payable	\$ 182,806	\$ 342,761
Accrued Expenses	201,368	202,036
Line of Credit	<u>117,000</u>	<u>189,699</u>
Total Liabilities	501,174	734,496
NET ASSETS:		
Unrestricted	1,001,103	781,289
Temporarily Restricted	75,383	95,164
Permanently Restricted	<u>1,000</u>	<u>1,000</u>
Total Net Assets	<u>1,077,486</u>	<u>877,453</u>
TOTAL LIABILITIES AND NET ASSETS	<u><u>\$ 1,578,661</u></u>	<u><u>\$ 1,611,949</u></u>

The Accompanying Notes are an Integral Part of the Financial Statements

HOME START, INC.
Statement of Activities
For the Year Ended June 30, 2008
(With Summary Totals for the Year Ended June 30, 2007)

	2008				2007
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total	Total
REVENUES:					
Subcontracts & Other Grants	\$ 4,412,742	\$	\$	\$ 4,412,742	\$ 4,511,088
Program Service Fees	332,023			332,023	317,681
Contributed Services	96,587			96,587	98,483
Contributed Materials	515,415			515,415	790,664
Contributions - Foundations	14,982	77,435		92,417	269,526
Contributions - Individuals & Other	30,158	56,860		87,018	89,756
Special Events	114,167			114,167	73,271
Interest & Other Income	13,073			13,073	2,400
Net Assets Released from Use Restrictions	154,076	(154,076)		-	-
Total Revenues	5,683,224	(19,781)	-	5,663,443	6,152,869
EXPENSES:					
Program Services					
Family Self-Sufficiency	1,314,812			1,314,812	2,807,927
Mental Health & Family Support	3,332,032			3,332,032	2,213,304
	4,646,844	-	-	4,646,844	5,021,231
Supporting Services					
Management & General	612,849			612,849	829,122
Fundraising & Development	203,717			203,717	153,833
	816,566	-	-	816,566	982,955
Total Expenses	5,463,410	-	-	5,463,410	6,004,186
Change In Net Assets	\$ 219,814	\$ (19,781)	\$ -	\$ 200,033	\$ 148,683
Beginning Net Assets	781,289	95,164	1,000	877,453	728,770
Ending Net Assets	\$ 1,001,103	\$ 75,383	\$ 1,000	\$ 1,077,486	\$ 877,453

The Accompanying Notes are an Integral Part of the Financial Statements

HOME START, INC.

Statement of Functional Expenses

For the Year Ended June 30, 2008

(With Summary Totals for Year Ended June 30, 2007)

EXPENSES	2008				2007	
	Family	Mental Health &	Program	Management	Fundraising	Total
	Self-Sufficiency	Family Support	Total	& General	& Development	
Payroll	\$ 385,114	\$ 1,650,953	\$ 2,036,067	\$ 309,823	\$ 105,382	\$ 2,451,272
Payroll Taxes	28,966	123,308	152,274	22,061	7,957	182,292
Benefits & Workers Comp	62,427	233,934	296,361	26,292	13,530	336,183
Subtotal Personnel	476,507	2,008,195	2,484,702	358,176	126,869	2,969,747
Clinical Supervision		45,355	45,355			45,355
Stipends		10,740	10,740			10,740
Subcontractors	65,781	657,705	723,486	41,461		764,947
Occupancy	58,014	173,527	231,541	35,689	11,598	278,828
Utilities	4,147	10,470	14,617	3,079	698	18,394
Communications	10,638	47,681	58,319	13,100	966	72,385
Repairs & Maintenance	14,349	46,176	60,525	20,804	3,017	84,346
Emergency Assistance	152,389	78,235	230,624			230,624
Consumables	4,357	40,828	45,185	13,352	14,413	72,950
Equipment Rental		6,745	6,745	11,338		18,083
Furniture/Equipment	1,413	12,299	13,712	1,295	1,450	16,457
Depreciation			-	19,348		19,348
Mileage	6,123	63,338	69,461	2,259	25	71,745
Travel		110	110			110
Meetings & Events	20	747	767	2,685	638	4,090
Seminars & Education	219	3,444	3,663	314	330	4,307
Legal & Accounting			-	24,206		24,206
Dues & Subscriptions	524	786	1,310	4,293	1,084	6,687
Donated Materials	514,416	999	515,415			515,415
Donated Services		96,419	96,419		168	96,587
Administrative Fees	3,895	15,895	19,790		350	20,140
Insurance			-	19,879		19,879
Recruitment	480	4,222	4,702	17,672	266	22,640
Special Events	45		45	2,286	34,514	36,845
Other	1,495	8,116	9,611	1,188	7,331	18,130
Interest Expense			-	20,425		20,425
Total Expenses	\$ 1,314,812	\$ 3,332,032	\$ 4,646,844	\$ 612,849	\$ 203,717	\$ 5,463,410
						\$ 6,004,186

The Accompanying Notes are an Integral Part of the Financial Statements

HOME START, INC.
Statement of Cash Flows
For the Year Ended June 30, 2008
(With Summary Totals for the Year Ended June 30, 2007)

	<u>2008</u>	<u>2007</u>
CASH FLOWS FROM OPERATING ACTIVITIES:		
Change in Net Assets	\$ 200,033	\$ 148,683
Adjustments to Reconcile Change in Net Assets		
To Net Cash Provided/Used by Operating Activities:		
Add back Depreciation	19,348	25,999
Decrease / (Increase) in:		
Accounts Receivable	42,227	(184,057)
Prepaid Expenses	27,167	(2,686)
Deposits	697	1,303
Increase / (Decrease) in:		
Accounts Payable	(159,955)	28,035
Accrued Expenses	(667)	11,576
Unearned Revenue and Contract Advances	<u>-</u>	<u>(58,653)</u>
Net Cash Provided (Used) by Operating Activities	<u>128,850</u>	<u>(29,800)</u>
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchase of Furniture and Equipment	-	(21,395)
Purchase of Leasehold Improvements	<u>-</u>	<u>(14,942)</u>
Net Cash Provided (Used) by Investing Activities	<u>-</u>	<u>(36,337)</u>
CASH FLOWS FROM FINANCING ACTIVITIES:		
Drawn on Line of Credit	2,640,779	1,932,810
Repayment of Line of Credit	<u>(2,713,478)</u>	<u>(1,992,300)</u>
Net Cash Provided (Used) by Financing Activities	<u>(72,699)</u>	<u>(59,490)</u>
Net Increase / (Decrease) in Cash and Cash Equivalents:	56,151	(125,627)
Cash and Cash Equivalents at:		
Beginning of Year	<u>10,519</u>	<u>136,146</u>
End of Year	<u>\$ 66,670</u>	<u>\$ 10,519</u>
Supplemental Disclosure of Cash Flow Information:		
Cash Paid for Interest	<u>\$ 20,425</u>	<u>\$ 30,964</u>

The Accompanying Notes are an Integral Part of the Financial Statements

HOME START, INC.
Notes to Financial Statements
June 30, 2008

Note 1. Organization

Nature of Organization

Home Start, Inc. (Home Start) is a not-for-profit corporation organized under the laws of the State of California. The agency has served San Diego County since 1972. Home Start is a community-based organization whose mission is to promote the safety and nurturance of children in San Diego County by fostering healthy families and communities. Home Start's programs focus on home-based services (mental health and family support, self-sufficiency, and adolescent support), center-based services, and community development.

These services are funded through a combination of Federal, California, and San Diego County contracts, program service fees, and public and private grants and donations.

Income Taxes

Home Start is exempt from income taxes in accordance with Section 501(c)(3) of the Internal Revenue Code, and Section 23701(d) of the California Revenue and Taxation Code.

Note 2. Summary of Significant Accounting Policies

Basis of Accounting

The financial statements are presented on the accrual basis, in accordance with U.S. generally accepted accounting principles. Under the accrual basis, revenues are recorded when earned and expenses are recorded when incurred, resulting in related receivables and payables.

Financial Statement Presentation

Home Start presents its financial statements in accordance with Financial Accounting Standards Board (FASB) Statement No. 117, *Financial Statements of Non-Profit Organization*, and the American Institute of Certified Public Accountants (AICPA) *Audit and Accounting Guide for Non-Profit Organizations*. These guides require that net assets, revenue, and expenses be classified as unrestricted, temporarily restricted, and permanently restricted based upon the following criteria:

Unrestricted Net Assets represent expendable funds available for operations, which are not otherwise limited by donor restrictions.

Temporarily Restricted Net Assets consist of contributed funds, subject to specific donor-imposed restrictions, contingent upon specific performance of a future event, or a specific passage of time before expenditure of funds.

Permanently Restricted Net Assets are subject to irrevocable donor restrictions, requiring that the assets be maintained in perpetuity, usually for generating investment income to fund current operations.

HOME START, INC.
Notes to Financial Statements
June 30, 2008

Note 2. Summary of Significant Accounting Policies (continued)

Cash and Cash Equivalents

Per the provisions of FASB Statement No. 96, *Statement of Cash Flows*, cash equivalents consist primarily of certificates of deposits and other securities with original maturities of 90 days or less.

Property and Equipment

Property and equipment purchased with Home Start funds are capitalized at cost. Donated equipment is recorded at estimated fair value. Home Start's policy is to capitalize acquisitions valued greater than \$2,000, unless the acquisitions are program expenditures covered by the program budget. In such cases, Home Start's management may choose to expense the acquisitions in the year of purchase. Depreciation is provided over the estimated useful lives or over the term of the respective assets on a straight-line basis as follows:

Furniture and equipment	5-7 years
Leasehold improvements	7-11 years
Vehicles	5 years

Unearned Revenue and Contract Advances

Home Start occasionally receives payments prior to performing services under contract agreements. These amounts are recorded as unearned revenue or contract advance liabilities until earned.

Donated Services, Materials, and Facilities

Donated services are recognized as contributions in the financial statements in accordance with FASB Statement No. 116, *Accounting for Contributions and Contributions Made*. If the contributed services (a) create or enhance non-financial assets, or (b) require specialized skills, are performed by individuals possessing those skills, and would typically need to be purchased if not provided by donation, then their fair value would be estimated and reported within the financial statements. Contributed materials, facilities, and other assets are recorded as contributions at their estimated fair values at the date of receipt or during the period of use where applicable.

Revenue Adjustments

Revenue under third-party reimbursement agreements is subject to retroactive audit adjustment. Provisions for estimated third-party settlements are recorded in the period the related services are rendered. Differences between estimated accruals and final settlements are recorded in the year of settlement.

Functional Allocation of Expenses

The costs of providing various programs and activities have been summarized on a functional basis in the statement of activities and the statement of functional expenses. Accordingly, certain costs have been allocated among programs and supporting services benefited.

HOME START, INC.
Notes to Financial Statements
June 30, 2008

Note 2. Summary of Significant Accounting Policies (continued)

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

June 30, 2007 Financial Information

The financial statements include certain prior-year summarized comparative information in total, but not by net asset class. Such information does not include sufficient detail to constitute a presentation in conformity with U.S. generally accepted accounting principles. Accordingly, such information should be read in conjunction with the audited financial statements for year end June 30, 2007 from which the summarized information was derived.

Note 3. Concentrations

Home Start maintains several bank accounts at Sunrise Bank of San Diego. During the year ended June 30, 2008, accounts were insured by the Federal Deposit Insurance Corporation up to \$100,000. At various times during the year, total cash maintained at Sunrise Bank may exceed the insured amount. Home Start has not experienced any losses in such accounts and the Board does not believe it is exposed to any significant credit risk on its cash and cash equivalents. Cash at Sunrise Bank did not exceed federally insured limits at June 30, 2008.

A significant portion of Home Start's revenue is provided by the County of San Diego, including Health and Human Services, and First 5 Commission. The County contracts with Home Start on an annual basis and has done so for 35 years. These programs are subject to annual evaluation of services rendered, and periodic monitoring reviews and directives.

Note 4. Accounts Receivable

At June 30, 2008, Home Start's receivables were principally comprised of contracts receivables and were stated at \$1,452,441. No allowance for uncollectible accounts has been established based on management's estimation that the amounts outstanding will be collected.

Contracts Receivable	\$1,056,802
Accrued Contracts Revenue	378,960
Pledges Receivable	13,568
Other	<u>3,111</u>
Total Accounts Receivable	<u>\$1,452,441</u>

HOME START, INC.
Notes to Financial Statements
June 30, 2008

Note 5. Line of Credit

Home Start has a \$450,000 revolving line of credit with Sunrise Bank of San Diego. The bank's Vice President of Business Development also serves on Home Start's Board of Directors. The line of credit is secured by substantially all of Home Start's assets and expires in April 2009. Interest only payments are due monthly. Interest is variable and is calculated based on the bank's prime rate plus one percent (5.5 percent at June 30, 2008). Outstanding balances are due 12 months from the date the funds were borrowed. At June 30, 2008, there was \$117,000 outstanding on the line of credit. Interest expense for the year ended June 30, 2008 was \$20,425.

Note 6. Accrued Leave Benefits

Accumulated unpaid employee vacation benefits are recognized as a liability of Home Start by multiplying the accumulated hours of accrued vacation benefits per employee times the hourly rate per employee. Home Start's policy is to allow employees to carry leave from one fiscal year to the next. For the year ended June 30, 2008, Home Start's accrued vacation pay liability totaled \$76,592.

Note 7. Retirement Plan and Benefits

Home Start has a defined 401(k) contribution plan that allows eligible employees who are over the age of 21 and have completed one year of service of at least 1,000 hours, to contribute up to 20 percent of their salary into the Plan, subject to annual limitations. Home Start may match 3 percent of the first 6 percent of employees' contributions. Home Start contributed \$12,102 for the year ended June 30, 2008.

Note 8. Contributed Services and Materials

The estimated fair value of qualified volunteer services is recorded in the financial statements. The value of the services has been calculated conservatively at the appropriate hourly rates. For the year ended June 30, 2008, the estimated value of the donated services by interns is \$96,587.

Home Start also received a substantial amount of donated materials, such as clothing and household items, which are used and distributed in programs. For the year ended June 30, 2008, Home Start has estimated the value of such donations at \$515,415.

HOME START, INC.
Notes to Financial Statements
June 30, 2008

Note 9. Operating Lease Commitments

Home Start leases its office facilities under non-cancellable operating leases expiring in August 2011 or prior. Home Start leases office equipment under long-term leases expiring in July 2012 or prior. For the year ended June 30, 2008, total office rent expense was approximately \$270,000 and equipment rent was approximately \$16,500. Future minimum lease payments for leases that have remaining terms in excess of one year at June 30, 2008 are as follows:

Years ending June 30,	
2009	199,775
2010	203,571
2011	194,836
2012	20,336
2013	<u>810</u>
Total	<u>\$ 619,328</u>

Note 10. Restricted Net Assets

Temporarily Restricted Net Assets at June 30, 2008 are:

Foundations	\$ 47,886
Individuals and Other	<u>27,498</u>
Total	<u>\$ 75,384</u>

Net assets released from donor restriction by incurring expenses:

Total	<u>\$154,076</u>
-------	------------------

Permanently Restricted Net Assets at June 30, 2008 are:

Katherine Kline Fund	<u>\$ 1,000</u>
----------------------	-----------------

Note 11. Related Parties

As discussed in Note 5, a member of Home Start's Board of Directors is also Vice President of Business Development of Sunrise Bank, the bank where Home Start maintains its operating bank accounts and from which Home Start has obtained a line of credit.

Another member of Home Start's Board of Directors provided design and printing services of the Organization's new logo and tag line, and complete redevelopment of the Organization's website. These services were provided at a cost of \$14,816 to the Organization.

HOME START, INC.
Supplemental Information
Schedule of Expenditures of Federal Awards
For the Year Ended June 30, 2008

<u>Program</u>	<u>Contract No.</u>	<u>Period</u>	<u>Total Award</u>	<u>CFDA</u>	<u>Expended</u>
U.S. Department of Health & Human Services					
Pass-through from the County of San Diego					
Housing & Community Development					
Family Self-Sufficiency - Central	46231	1/1/07 - 12/31/07	658,277	93.569	\$ 149,722
Family Self-Sufficiency - Central		1/1/08 - 12/31/08	635,151	93.569	413,443
Family Self-Sufficiency - East	46228	1/1/07 - 12/31/07	302,037	93.569	59,856
Family Self-Sufficiency - East		1/1/08 - 12/31/08	282,826	93.569	185,714
Health & Human Services Agency					
Community Services for Families - East	504311	7/1/07 - 6/30/08	1,143,025	93.556	1,128,416
Financial Literacy (LITC)	21008	1/1/07 - 12/31/07	16,000	93.995	7,813
Financial Literacy (LITC)		1/1/08 - 12/31/08	13,000	93.995	8,526
Medi-Cal Administrative Activities (MAA)	03-75085	4/1/05 - 6/30/06	308,634	93.778	308,634
Pass-through from North County Lifeline					
Community Services for Families - North Inland	504335	7/1/07 - 6/30/08	257,292	93.556/93.590	260,341
Community Services for Families - North Coastal	504335	7/1/07 - 6/30/08	249,042	93.556/93.590	261,720
Pass-through from Social Advocates for Youth San Diego, Inc. (SAY)					
Community Services for Families - Central	504321	7/1/07 - 6/30/08	310,352	93.556	304,165
Total U. S. Department of Health & Human Services					<u>3,088,350</u>
U.S. Department of Justice					
Pass-through from the State of California					
CHAT - SD	AT 05-02-1373	10/1/06 - 9/30/07	207,810	16.575	90,393
CHAT - SD	AT 05-02-1373	10/1/07 - 9/30/08	200,000	16.575	141,190
Total U. S. Department of Justice					<u>231,583</u>
Total Expenditures of Federal Awards					<u><u>\$3,319,933</u></u>

Note 1. Basis of Presentation

This schedule is prepared on the accrual basis of accounting except in the case of the Medi-Cal Administrative Activities (MAA) award which is reported on the cash basis. Because of delays in billing required by Home Start's contract with the County of San Diego, MAA receipts are not billed until at least one year after the related period and the collectible portion is not known until after billing is complete. The Total Award and Expended amounts above include MAA receipts collected from the County during the year ended June 30, 2008 for reimbursement of expenditures related to the period of April 1, 2005 through June 30, 2006.

Note 2. Sub-recipients

Home Start, Inc. passed federal awards to sub-recipients as follows:

Family Self-Sufficiency (FSS)	93.569	65,781
Community Services for Families - East	93.556	631,951
Total Sub-recipient Payments		<u>\$ 697,732</u>

See Auditor's Report on Compliance



Sonnenberg & Company, CPAs

A Professional Corporation

5190 Governor Drive, Suite 201, San Diego, California 92122

Phone: (858) 457-5252 • (800) 464-4HOA • Fax: (858) 457-2211 • (800) 303-4FAX



Leonard C. Sonnenberg, CPA

Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*

To the Board of Directors of
Home Start, Inc.

We have audited the financial statements of Home Start, Inc. (a Nonprofit Organization) as of and for the year ended June 30, 2008, and have issued our report thereon dated October 30, 2008. We conducted our audit in accordance with U.S. generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Home Start's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of its internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Organization's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

A *control deficiency* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A *significant deficiency* is a control deficiency, or combination of control deficiencies, that adversely affects the Organization's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles, such that there is more than a remote likelihood that a misstatement of the Organization's financial statements that is more than inconsequential will not be prevented or detected by the Organization's internal control. We consider the deficiencies described in the accompanying Schedule of Findings and Questioned Costs to be significant deficiencies in internal control over financial reporting. Significant deficiencies are described in the accompanying Schedule of Findings and Questioned Costs as item(s) **2007-01, 2008-01**.

A *material weakness* is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the Organization's internal control.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, we believe that the significant deficiencies described above are not a material weakness.

**Report on Internal Control over Financial Reporting and on Compliance and Other Matters
Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing
Standards* (Continued)**

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Home Start's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of the Audit Committee, Board of Directors, management, awarding agencies, and pass-through entities and is not intended to be, and should not be, used by anyone other than these specified parties.

October 30, 2008


Sonnenberg & Company, CRAs



Sonnenberg & Company, CPAs

A Professional Corporation

5190 Governor Drive, Suite 201, San Diego, California 92122

Phone: (858) 457-5252 • (800) 464-4HOA • Fax: (858) 457-2211 • (800) 303-4FAX



Leonard C. Sonnenberg, CPA

Report on Compliance with Requirements Applicable to Each Major Program and Internal Control over Compliance in Accordance with OMB Circular A-133

To the Board of Directors of
Home Start, Inc.

Compliance

We have audited the compliance of Home Start, Inc. with the types of compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that are applicable to each of its major federal programs for the year ended June 30, 2008. Home Start's major federal programs are identified in the summary of auditor's results section of the accompanying Schedule of Findings and Questioned Costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of Home Start's management. Our responsibility is to express an opinion on Home Start's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about Home Start's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of Home Start's compliance with those requirements.

In our opinion, Home Start, Inc. complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended June 30, 2008.

Internal Control over Compliance

The management of Home Start, Inc. is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered Home Start's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of Home Start's internal control over compliance.

Report on Compliance with Requirements Applicable to Each Major Program and Internal Control over Compliance in Accordance with OMB Circular A-133 (Continued)

A *control deficiency* in an entity's internal control over compliance exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect noncompliance with a type of compliance requirement of a federal program on a timely basis. A *significant deficiency* is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to administer a federal program such that there is a more than a remote likelihood that noncompliance with a type of compliance requirement of a federal program that is more than inconsequential will not be prevented or detected by the entity's internal control.

A *material weakness* is a significant deficiency, or a combination of significant deficiencies, that results in a more than remote likelihood that material noncompliance with a type of compliance requirement of a federal program will not be prevented or detected within a timely period by the entity's internal control. We do not consider any of the deficiencies described in the accompanying Schedule of Findings and Questioned Costs to be material weaknesses.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above.

Schedule of Expenditures of Federal Awards

Our audit was performed for the purpose of forming an opinion on the basic financial statements of Home Start, Inc. taken as a whole. The accompanying Schedule of Expenditures of Federal Awards is presented for purposes of additional analysis as required by U. S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

This report is intended solely for the information and use of the Audit Committee, Board of Directors, management, awarding agencies and pass-through entities, and is not intended to be, and should not be, used by anyone other than these specified parties.



Sonnenberg & Company, CPAs

October 30, 2008

HOME START, INC.
Schedule of Findings and Questioned Costs
For the Year Ended June 30, 2008

Summary of Auditor's Results

1. The auditor's report expressed an unqualified opinion on the financial statements of Home Start, Inc. (the Organization).
2. Significant deficiencies related to the audit of the financial statements are reported in the Report on Internal Control over Financial Reporting and on Compliance and Other Matters based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards* and further described below.
3. No instances of noncompliance material to the financial statements of Home Start, Inc. were disclosed during the audit.
4. No significant deficiencies related to the audit of the major federal award programs were disclosed during the audit.
5. The auditor's report on compliance expresses an unqualified opinion for all major federal programs.
6. Audit findings that are required to be reported in accordance with Section 510(a) of OMB Circular A-133 are reported in this Schedule.
7. The programs tested as major programs include: Community Services Block Grant (CFDA No. 93.569), Promoting Safe and Stable Families (CFDA No. 93.556), and Medical Assistance Program (CFDA No. 93.778).
8. The threshold used for distinguishing between Type A and B programs was \$300,000.
9. Home Start, Inc. qualified as a low-risk auditee.

Findings – Financial Statements Audit

Significant Deficiencies

2007-01 Personnel Turnover

Criteria: Turnover in key positions can adversely affect the effectiveness of an Organization's internal control system because (a) if control procedures are not sufficiently documented, knowledge may be lost, (b) hiring and training are time consuming activities which put a strain on employees who are already affected by the vacancy, (c) the relative inexperience of a new employee increases the possibility for errors, and (d) the new employee may not have the experience or expertise to be effective in his/her new role.

Statement of Condition: The Director of Business and Finance (Director) is charged with financial reporting for the Organization, including responsibility for cost allocations and financial reporting. There are numerous cost centers, making it difficult to manage and allocate expenses and accurately report expenses by cost center.

Findings: In Fall 2007, the Director was simultaneously gaining familiarity with the Organization's financial management while assisting with the annual audit, and had not had time to analyze the cost allocations and departmental reporting. As a result, some cost centers may not be charged all of their proper expenses, while others are carrying those expenses.

Recommendations: We recommend that the Director continue to work with the accounting system to improve cost allocations and financial reporting for management's information. It may be helpful to bring in a consultant who specializes in the Organization's particular accounting software.

2008 Update: The Organization has continued to experience a high degree of turnover in the Director of Business and Finance position: to the extent that the Organization operated without someone in that position for several months during the year ended June 30, 2008. To mitigate the effect the vacancy had on internal controls, a Board member completed some of the Director duties during that period. Nonetheless, the results of our audit indicate that the turnover in the Director position, when coupled with turnover in other positions in the finance department, has caused an apparent loss of Organization-specific knowledge related to fixed asset depreciation and other functions. The current Director of Business and Finance has a strong familiarity with the accounting software and has expressed intentions to make specific changes to the Organization's cost allocation method, which should improve management's ability to evaluate the success of each program and the Organization's development needs. We feel when the Director evaluates the finance department staff he needs to determine the suitability of assignments and/or whether improved training is needed in some areas. We also believe the underlying risks associated with the turnover, as described above, will continue until the position is held by the same individual for at least one year and/or a sense of routine has been established.

View of Responsible Officials: Home Start concurs with the recommendation. The various concerns of budget, cost allocations, and supervision of the finance staff can be solved by having a qualified individual remain at the position for a minimum of at least a year. While several factors have contributed to the lack of retention for this position, Home Start remains committed to doing everything within its power to retain all qualified personnel, including the Director of Business and Finance position.

2008-01 Control over Receipts

Criteria: An Organization's management is responsible for the design and implementation of internal controls that allow management or employees, in the normal course of performing their assigned functions, to detect or prevent misstatements on a timely basis.

Statement of Condition: Home Start's administrative staff person is tasked with opening the mail, date stamping receipts that are received and forwarding them to the finance department for processing. The receipts are not entered into the general ledger until the bank returns a deposit receipt.

Findings: The results of our testing suggest that the practice of date stamping receipts is not consistently applied. Furthermore, because two people do not open the mail and no receipt log is kept, the risk of misappropriation of receipts that arrive in the mail is greater than necessary.

Recommendations: Best practices would involve two people opening the mail, logging receipts that are received, and providing that log to the Accounting Manager who posts the receipts after they are deposited so that receipts that are deposited can be cross-referenced with those received.

View of Responsible Officials: Home Start concurs with the recommendation. All mail will be date stamped and opened by two personnel. A receipt log will be generated to document all funds received and forwarded to the Accounting Manager who will be able to post the receipts once the deposits are cross-referenced against the receipt log.

Material Weaknesses

We identified no control deficiencies that constitute material weaknesses.

Findings and Questioned Costs – Major Federal Award Programs

Significant Deficiencies

We identified no control deficiencies that constitute significant deficiencies.

Material Weaknesses

We identified no control deficiencies that constitute material weaknesses.

MANAGEMENT ADVISORY LETTER

November 12, 2008

To the Board of Directors
and Chief Executive Officer of Home Start, Inc.

We have presented your audited financial statements for the year ended June 30, 2008 in a comparative accounting format recommended by the AICPA Audit and Accounting Guide for Not-For-Profit Organizations. This letter does not affect our report dated October 30, 2008 on the financial statements or our Single Audit reports.

In planning and performing our audit of the financial statements, we considered the Organization's internal control to determine our auditing procedures for the purpose of expressing an opinion on the financial statements and not to provide assurance on internal control.

However, during our audit we became aware of several matters that are opportunities for strengthening internal controls and operating efficiency. Significant deficiencies (and material weaknesses, if any) identified during our audit of your financial statements have been communicated under separate cover. The Specific Recommendations that accompany this letter detail areas we noted during our audit that if improved would increase the Organization's efficiency, accuracy, ability to safeguard of assets, and enrich the information provided to management.

The Standard Recommendations and Tax Information that accompany this letter summarize our suggestions and regulations that apply to most non-profit organizations.

We wish to thank the Chief Executive Officer and staff for the cooperation they provided to us. We have been pleased to be retained as your auditing firm.

Very truly yours,

Sonnenberg & Company, CPAs

SPECIFIC RECOMMENDATIONS

Accounting Procedures Manual

Finding: The Organization's Accounting Policies and Procedures manual, which was last revised in 2004, focuses on special case expenditures (e.g.; petty cash, credit card use, and employee reimbursement) and appears to be designed for use by employees outside of the finance department in preparing the paperwork to support their transactions. The Organization does not have a manual that documents the finance department's activities, responsibilities, and control procedures.

Recommendations: Home Start's management is tasked with ensuring that the Organization's internal control system is properly designed and effectively implemented. To improve management's effectiveness and formalize the accounting procedures, we recommend that the Organization develop an accounting policies and procedures manual, which should summarize the functions of the finance department and highlight the Organization's considerations of the five (5) elements of internal control (environment, risk assessment, information/communication systems, monitoring, and control activities) in relation to those functions.

Fixed Asset Capitalization

Finding: Likely because of the high turnover in the Director of Business and Finance position, the finance department personnel appear uncertain about whether purchases of equipment should be capitalized when funds for that equipment are included in a program's budget. Additionally, the fixed asset depreciation schedule that was provided to us for audit did not tie to the same schedule that was provided for the 2007 audit, not did it support the financial statements at June 30, 2008.

Recommendations: We recommend that the Organization develop a policy related to capitalization of program-specific equipment purchases. Considerations should be made regarding the ease of misappropriation, specific identification, and tracking, potential for administrative uses or use in other programs, and particulars of the contract (e.g.; is Home Start required to surrender the equipment to the funding agency if still in use at the end of the program?). Determinations will likely be made on a case-by-case basis, but formalizing the criteria used in making the determination would ease uncertainty and ensure that the capitalization policy is being consistently applied.

Additionally, efforts should be made to reconcile the fixed asset depreciation schedule to the financial statements on a regular basis (e.g.; monthly or quarterly). Procedures should be in place to ensure that the schedule is updated whenever fixed assets (that are to be capitalized) are purchased, depreciation is recorded, and fixed assets are retired, sold, or otherwise disposed of.

In-Kind Donations

Finding: Contributed Materials - The Organization's in-kind donations of goods are valued by the donor. Contributed Facilities - The Organization receives donations of facilities (the use of an office, desk, or similar) from its program partners, which have not been valued by the Organization. Based on inquiry we believe the value of donated facilities to be insignificant to the financial statements.

Recommendations: Contributed Materials - Because donors of in-kind goods have a motive to inflate the value of their donations, we recommend that a procedure be implemented (probably within the warehouse) to document an evaluation of the appropriateness of the donor's valuation. Contributed Facilities - We recommend that the staff member in charge of maintaining the Organization's lease schedule also document the donated facilities and approximate value where possible (either under separate cover or within the same schedule). If Home Start is paying a reduced fee for services from certain subcontractors because of the exchange of donated facilities, the actual value of the services should be determined in order to determine the value of donated facilities.

Formalization of Controls over Compliance with Program Requirements

Findings: During the course of our audit we noted that the Director of Programs has developed a reliable system of ensuring Program Managers and staff are successful in achieving the objectives of the contracts. However, because the Director has been in the position for some time, and developed this system over that period, the control system is not documented in any formal, generalized way.

Recommendations: We recommend developing a manual or handbook that highlights the Organization's consideration of the five (5) elements of internal control (see Accounting Manual above) as it relates to compliance with program requirements and documents the ways in which the Director of Programs and the staff ensure program activities support the achievement of control goals.

TAX INFORMATION – NEW AND UPDATED 2008

Sales Tax and Use Tax: Although many organizations are exempt from federal and state income taxes, there is no similar general exemption from California sales tax and use tax. Nonprofit groups' sales may be taxable even though the proceeds are used for philanthropic purposes. Likewise, nonprofit groups' purchases may be taxable even though the purchaser is engaged in charitable activities.

Most nonprofits are aware they incur taxable sales if they operate some type of store or ongoing sales activity. Taxable activities commonly engaged in by nonprofit and volunteer organizations include:

- Sales of food, meals, beverages, and so forth, under certain circumstances
- Sales of items at rummage sales, bazaars, carnival booths, auctions, silent auctions, community events, and other fundraisers. Tax applies to the sale of homemade items, commercially produced goods, and donated merchandise.
- Ticket charges for game booths where prizes are guaranteed to each ticket purchaser, even though the prizes may have little value. White elephant, fish pond, grab bag, are examples of taxable game booth activities.

Taxable sales require you to apply for a seller's permit, collect sales tax, remit sales tax, and submit sales tax returns. If working with a fundraising company, they may be responsible for those activities on your behalf.

Many smart shoppers can find bargains online, but don't realize they can incur a tax bill in the process for "Use tax". California law requires tax on in-state purchases, and also requires tax on items purchased out-of-state for use in California.

For more information, we encourage you to visit the California Board of Equalization website and download Publication 18 "Tax Tips for Nonprofit Organizations." It is full of useful explanations, examples, exclusions, etc. Information on Use Tax can be found at <http://www.boe.ca.gov/ads/news06.htm>.

Property Tax: Nonprofit organizations that own property can receive property tax exemptions. The Board of Equalization (Board) and the county assessor jointly administer the Welfare and Veterans' Organization Exemptions. The Board determines whether the organization is eligible to receive the welfare or veterans' organization exemption; and if eligible, issues an Organizational Clearance Certificate for the claimant to provide with claim forms filed in any of the 58 counties. The county assessor determines whether the use of the property is eligible for the exemption. Applications for exemption of property are filed with the county assessor where the property is located. The assessor is responsible for granting or denying exemption.

Note that some nonprofits may receive partial exemptions, if not all of the land is used for nonprofit activities. For applications and more information, visit <http://www.boe.ca.gov/proptaxes/welfarevets.htm>.

Unrelated Business Income Tax: Most income received by nonprofit organizations is considered exempt from income taxes. However, sometimes there is "unrelated business income" which is subject to "unrelated business income tax" (UBIT). Nonprofits should regularly review their income to determine if they have incurred UBIT.

An activity is an unrelated business if it meets three requirements:

1. It is a trade or business,
2. It is regularly carried on, and
3. It is not substantially related to furthering the exempt purpose of the organization.

If the nonprofit has unrelated business income, they are required to pay taxes at standard corporation tax rates, as well as file IRS form 990-T and FTB form 109.

There are, however, a number of modifications, exclusions, and exceptions to the general definition of unrelated business income. For example, dividends, interest, certain other investment income, royalties, certain rental income, certain income from research activities, and gains or losses from the disposition of property are excluded when computing unrelated business income.

In addition, the following activities are specifically excluded from the definition of unrelated trade or business:

- **Volunteer Labor:** Any trade or business is excluded in which substantially all the work is performed for the organization without compensation. Some fundraising activities, such as volunteer operated bake sales, may meet this exception.
- **Convenience of Members:** Any trade or business is excluded that is carried on by an organization described in section 501(c)(3) or by a governmental college or university primarily for the convenience of its members, students, patients, officers, or employees. A typical example of this is a school cafeteria.
- **Selling Donated Merchandise:** Any trade or business is excluded that consists of selling merchandise, substantially all of which the organization received as gifts or contributions. Many thrift shop operations of exempt organizations would meet this exception.

For additional information, visit www.irs.gov and download Publication 598, “Tax on Unrelated Business Income of Exempt Organizations.”

Employment Tax - W-2 vs. 1099: Before a tax-exempt organization (EO) can determine how to treat payments for services rendered, the EO must first know the business relationship that exists between the organization and the person performing the services. The person performing the services may be:

- An independent contractor,
- A common-law employee (employee),
- A statutory employee, or
- A statutory non-employee.

In determining whether the person providing the service is a common law employee or an independent contractor, all information that provides evidence of the degree of control and independence must be considered.

It is critical that the EO, as the employer, correctly determine whether individuals providing services are employees or independent contractors. Generally, the EO must withhold income taxes, withhold and pay Social Security and Medicare taxes, and pay unemployment tax on wages paid to an employee. The EO does not generally have to withhold or pay any taxes on payments to independent contractors.

Under IRS guidelines, an officer of a nonprofit is a “statutory employee” per IRS Publication 15-A:

An officer of a corporation is generally an employee; however, an officer who performs no services or only minor services, and neither receives nor is entitled to receive any pay, is not considered an employee. **A director of a corporation** is not an employee with respect to services performed as a director.

This can become confusing, because the term “officer” and “director” are often used interchangeably to describe persons serving as staff AND persons serving as Board members. However, it is generally interpreted to include: CEO/Executive Director, CFO/Controller, and any Board officers compensated for services.

An EO can be held liable for employment taxes, plus interest and penalties, if a worker is incorrectly classified as an independent contractor. Also, see www.irs.gov and lookup Paying Independent Contractors for information on reporting requirements for payments to independent contractors.

Refer to **Who Are Employees?** in IRS Publication 15-A, *Employer's Supplemental Tax Guide*, for more information. See also IRS publication “Employment Tax Resources for Exempt Organizations,” for more information. Also, there are many versions of the IRS “20-factor test” that you can use to determine the employment status, such as: <http://www.taxprophet.com/apps/active2/indep-mm.html>

Raffles & California Law: In California, charities and certain other private nonprofit organizations may conduct raffles (including opportunity drawings) to raise funds for beneficial or charitable purposes in the state. This exception to the general constitutional prohibition against lotteries requires that at least 90 percent of the gross receipts from these raffles go directly to beneficial or charitable purposes in California. What organizations qualify and how the raffles must be conducted are governed by Penal Code section 320.5, which was added by Senate Bill 639 (McPherson, Chapter 778, Stats. of 2000). For details, view the Frequently Asked Questions <http://ag.ca.gov/charities/faq.php>

Unless specifically exempted, a nonprofit organization must register with the Attorney General's Registry of Charitable Trusts prior to conducting the raffle and file financial disclosure reports on each raffle event. There are two reports required:

- Nonprofit Raffle Registration Form - CT-NRP-1 - Each nonprofit organization that intends to conduct a raffle during a year (September 1 through August 31) must complete and submit a raffle registration form. A \$20 filing fee is required.
- Nonprofit Raffle Report - CT-NRP-2 - A nonprofit organization that has registered to conduct a raffle must file a separate nonprofit raffle report for each raffle held during the year (September 1 through August 31).

These forms are provided at: <http://caag.state.ca.us/charities/raffles.htm>.

FDIC Limits: The AICPA requires that auditors disclose a risk of loss in the notes the financial statements if cash balances exceed the \$100,000 limit. This requirement has been in effect for years, but is gaining more attention as the banking industry has begun to struggle. Many of our clients are re-evaluating their bank accounts to determine if funds should be re-allocated to insure adequate protection.

The FDIC – short for the Federal Deposit Insurance Corporation - is an independent agency of the United States government. The FDIC protects depositors against the loss of their insured deposits if an FDIC-insured bank or savings association fails. FDIC insurance is backed by the full faith and credit of the United States government.

If a depositor's accounts at one FDIC-insured bank or savings association total \$100,000 or less, the deposits are fully insured. A depositor can have more than \$100,000 at one insured bank or savings association and still be fully insured provided the accounts meet certain requirements. In addition, federal law provides for insurance coverage of up to \$250,000 for certain retirement accounts.

The FDIC website provides a list of failed banks, a calculator of your insured risk, and more information. See www.fdic.gov for more information.

STANDARD RECOMMENDATIONS

Audit and/or Finance Committee: The Board of Directors should consider appointing an Audit Committee in order to have direct, confidential communication with the independent auditor. The Audit Committee should have qualified persons with financial experience, and should not include the Executive Director, CFO, or other employees. A Finance Committee is recommended to consider financial oversight of operations, investment policies, major fund-raising, and long-range planning. The Finance Committee should have qualified persons with financial expertise, and should not have a majority of staff members.

Conflict of Interest Policy: The Board of Directors is required by California Corporation Code 7233 to disclose any conflicts of interest. The IRS asks questions about the Conflict of Interest policy starting with the 2007 Form 990. Therefore, we recommend that the Organization adopt a formal conflict of interest policy aimed at preventing or resolving issues related to potential or actual conflict of interest issues. In addition, the Board and management should be educated about ethics, disclosure, and independence in order to prevent related party transactions, self-dealing, private inurement, and similar issues. If they exist, these transactions must be disclosed to the auditor and, if significant, in the audit report. Such transactions are often scrutinized by the IRS and Attorney General and may be disallowed if the amounts and the business purpose are not clearly identifiable.

Fraud: In 2002, AICPA issued SAS 99, *Consideration of Fraud in a Financial Statement Audit*, requiring auditors to increase their procedures to detect fraud and to discuss the possibility for fraud with the client during the audit. The Board of Directors, management, and employees are encouraged to contact the auditor if they feel fraud exists or could potentially exist. However, an audit is still not guaranteed to detect fraud, even if it exists. Management and the Board of Directors are responsible to design internal controls that protect against fraud.

In-kind Donations: Many nonprofit Partnerships receive significant amounts of donated materials, property, and services. Often, these donations have a financial value that can be recorded in the financial statements if accurate records are provided to the auditor:

- Donated Materials: Description, date received, estimated fair market value
- Donated Property: Description, date received, estimated fair market value
- Donated Services: Description, number of hours, estimated hourly rate, program benefited

Insurance: Insurance coverage should be reviewed annually to ensure adequate coverage types and amounts, including General Liability, Professional Liability, Property, Directors & Officers, Volunteers, Special Events, etc. Directors and Officers coverage would protect the Organization and individual board members and officers from personal liability for lawsuits against the Organization. All other insurance coverage should be reviewed annually to ensure adequate coverage. The additional cost of insurance may be negligible when compared to the liability exposure.

Investment Policy: The Board should consider adopting a formal investment policy aimed at guiding management in issues related to investment risk, authorization, limits, and related issues.

Minutes: Board of Directors meetings should be held regularly and proper minutes should be kept of all meetings. These minutes should indicate that the Board documents significant financial information, such as: approval of the budget, financial statements, replacement fund transactions, write-offs of uncollectible receivables, capital expenditures, contract approvals, related party transactions, insurance settlements, and litigation matters.

Nonprofit Integrity Act: This landmark legislation went into effect January 1, 2005. Most nonprofit organizations in California are impacted, with a few exceptions: religious organizations, educational institutions, and hospitals. There are two parts to the legislation and there are some financial thresholds for some provisions:

1. All Charities
 1. Accelerated Registration Requirements: Must register with Attorney General within 30 days of operations
 2. Executive compensation must be reviewed and approved by the Board
 3. Audit Public Disclosure. If already having an audit, must provide upon request, same as Form 990
2. Charities with Gross Revenue over \$2 million (excludes government grants)
 1. Independent audit required
 2. Auditor Independence standards set by Government Auditing Standards
 3. Audit Public Disclosure. Must provide upon request, same as Form 990. Due no later than 9 months after FYE
 4. Audit Committee Required: Must be independent of Finance Committee, cannot include CEO, CFO, Executive Director, Staff, Finance Committee Chair.
 5. Audit Committee Duties: Recommend hiring/firing of auditor, confer with auditor regarding financial affairs, must review and approve audit, approve non-audit services. Cannot be same as Finance Committee.
3. Applies to Charitable Partnerships, Commercial Fundraisers, Fundraising Counsel
4. Twelve Prohibited Acts. Generally: do not mislead, misrepresent, misappropriate, over estimate, exploit or commit fraud

Tax Returns - Increased Scrutiny: Non-profit Organizations must file annual exempt organization tax returns to report on financial activities as well as changes within the Organization, fundraising, lobbying, compensation, etc. In 2004, the IRS and California Attorney General announced plans to hire additional auditors to audit more exempt organization returns. California's new Nonprofit Integrity Act will focus on governance, i.e. adequate oversight by the Board. In particular, the two agencies are focusing on:

- IRS: political activities, tax shelters, excessive compensation packages, donated property transactions (vehicles, land, buildings).
- California Attorney General: Executive compensation, public disclosure of audits, commercial fundraising, audit committees, raffles.

Further, public access to nonprofit returns via GuideStar means that anyone can look at your 990 at any time. Professional, complete, and accurate tax preparation is vital to your organization's image.

Tax Returns - Client Preparation: Even with tax preparation by your auditor, the nonprofit must provide certain information that cannot be obtained from basic financial records. Nonprofits should be prepared to provide this critical information at tax time:

- List of Board Members: name, title, hours worked, compensation, expense account
- List of Contributors that gave over \$5,000: Name, address, amount. This information is NOT public information and is blocked out on GuideStar.
- Operating Questions: Page 5 of the 990 and Form RRF1 contain a long list of questions regarding operations, disclosures, in-kind donations, relationships with other nonprofits, related parties, fraud, political activity



Main Office

5005 Texas Street
Suite 203
San Diego, CA 92108
Tel: (619) 692-0727
Fax: (619) 692-0785

Mid-City Office

5296 University Ave.
Suite F-2
San Diego, CA 92105
Tel: (619) 229-3660
Fax: (619) 265-2408

East County Office

338 W. Lexington Avenue
Suite 105
El Cajon, CA 92020
Tel: (619) 401-8375
Fax: (619) 401-5321

North Coastal Office

1320 Union Plaza Court
Oceanside, CA 92054
Tel: (760) 439-7513
Fax: (760) 439-5625

North Inland Office

463 N. Midway Drive
Suite 200
Escondido, CA 92027
Tel: (760) 489-4951
Fax: (760) 489-4811

March 25, 2009

Local Assistance Monitoring Branch
Governor's Office of Emergency Services
3650 Schriever Avenue
Mather, CA 95655

Ref: 2008 Annual Audit Report and Corrective Action Plan (CAP)

To Whom It May Concern,

Included is (1) copy of our Audited Financial Statements and Single Audit Reports and (1) copy of the Management Advisory Letter.

Additionally, the Schedule of Findings and Questioned Costs on pages 16-18 of the audit identify Personnel Turnover (2007-01) and Control over Receipts (2008-01) as items of concern, and the Corrective Action Plan (CAP) is noted as such:

2007-01 – The Director of Business and Finance will be evaluated by the CEO through performance evaluations. For the current year, the CEO will be having a mid-year evaluation of the individual (May 11th, 2009), with subsequent yearly evaluations occurring at the hiring anniversary date (per Home Start policy).

2008-01 – Shortly after the auditor's completion of the audit, the Director of Business and Finance implemented the new protocol recommended by the auditor (December 2nd, 2008). "All mail will be date stamped and opened by 2 personnel. A receipt log will be generated to document all funds received and forwarded to the Accounting Manager who will be able to post once the deposits are cross-referenced against the receipts."

Please let us know if there are any other questions in relation to the audit and/or management letter.

Sincerely,

Bryce Guthrie
Director of Business and Finance

Cc: Laura Mustari, CEO